Airlie Australian Share Fund
(Managed Fund)

A concentrated, active portfolio of Australian equities.
Accessing the Airlie investment team and Magellan's operational and client services capabilities.

Airlie Funds Management

Ticker: AASF

Fund Update: 31 March 2023 ARSN: 623 378 487

FUND FACTS

Investment Objective: To provide long-term capital growth and regular income through investment in Australian equities.

Investment Strategy
- Long only, bottom up specialised and focused Australian equities fund
- Concentrated portfolio of 15-35 stocks (target 25)
- Active, high conviction approach - Airlie's 'best ideas'

Inception Date	1 June 2018	
Benchmark	S&P/ASX 200 Accum. Index	
Portfolio Size	AUD $349.4 million	
Distribution Frequency	Semi-annually	
Management Fee	0.78% p.a. (inclusive of net effect of GST)	
Ticker	AASF	
Tickers	**Solactive**	**ICE**
Bloomberg (AASF AU Equity)	AASFAUIV	AASFIV Index
Thompson Reuters (AASF.AX)	AASFAUDINAV=SOLA	AASFAUiv.P
IRESS (AASF.AXW)	AASFAUDINAV	AASF-AUINAV.NGIF
APIR	MGE9705AU	
Minimum Initial Investment#	AUD$10,000	
Buy/Sell Spread#	0.14%/0.14%	

WHY CHOOSE THE AIRLIE AUSTRALIAN SHARE FUND?

- Access to an experienced, proven investment team specialising in Australian Equities, with a long track record of prudent common-sense investing
- A conservative and robust investment process that focuses the team's energies on their best ideas
- The strategy is now available to retail investors for the first time through the partnership with Magellan

PORTFOLIO MANAGERS

Emma Fisher
Over 13 years investment experience. Formerly an investment analyst within the Australian equities team at Fidelity International and prior to that Nomura Securities.

Matt Williams
Over 30 years investment experience. Formerly Head of Equities and portfolio manager at Perpetual Investments.

Visit www.airlieaustraliansharefund.com.au for more information, including: fund performance, unit prices and iNAV, investment insights, PDS, TMD & forms

 # only applicable to investors who apply for units directly with the fund.

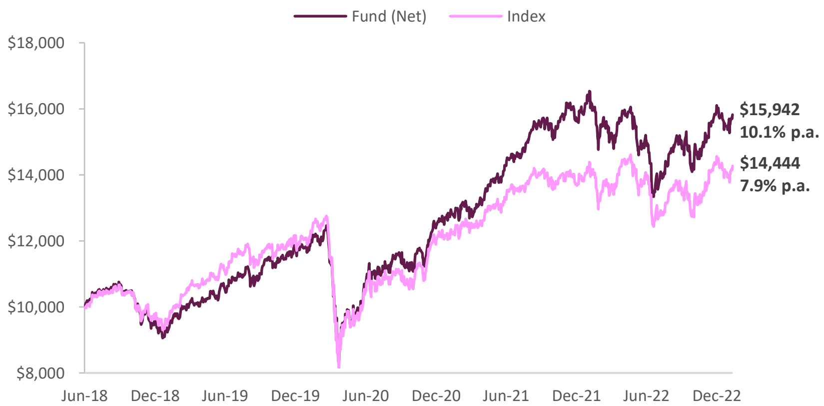
PERFORMANCE*

	Fund (%)	Benchmark (%)	Excess (%)
1 Month	-0.7	-0.2	-0.5
3 Months	3.5	3.5	0.0
6 Months	12.5	13.2	-0.7
1 Year	0.2	0.1	0.1
3 Years (p.a.)	20.2	16.5	3.7
4 Years (p.a.)	12.0	7.9	4.1
Since Inception (p.a.)	10.1	7.9	2.2

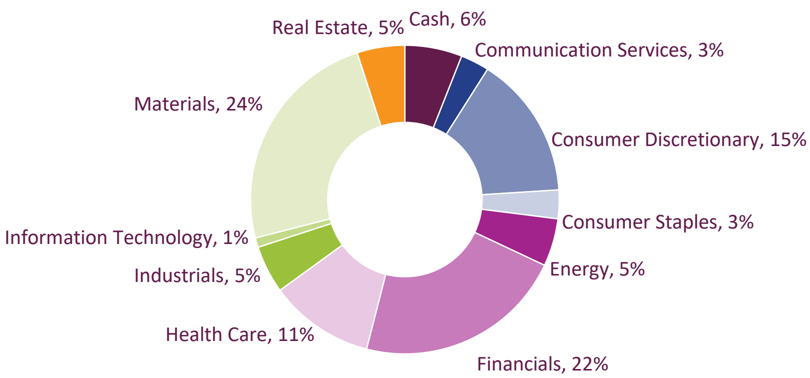
TOP 10 POSITIONS (BY WEIGHT)

Company	Sector**
BHP Group Ltd	Materials
CSL Ltd	Health Care
Commonwealth Bank of Australia	Financials
Mineral Resources Ltd	Materials
National Australia Bank Ltd	Financials
Macquarie Group Ltd	Financials
Medibank Pvt Ltd	Financials
Wesfarmers Ltd	Consumer Discretionary
Tabcorp Holdings Ltd	Consumer Discretionary
James Hardie Industries Plc	Materials

PERFORMANCE CHART GROWTH OF AUD $10,000*



PORTFOLIO POSITIONING**



* Calculations are based on exit price with distributions reinvested, after ongoing fees and expenses but excluding individual tax, member fees and entry fees (if applicable). Returns denoted in AUD.
** Based on GICS Sector classification, may not sum to 100% due to rounding.

MARKET COMMENTARY

The Airlie Australian Share Fund rose 3.53% for the quarter, slightly outperforming the ASX 200 index, which rose 3.46%. Overall, a reasonably strong quarter for the local market, as global markets speculated that the co-ordinated aggressive central bank tightening cycle was near a peak. This view was hastened somewhat as the US regional bank crisis and emergency takeover of Credit Suisse occurred late in the quarter. Contagion to a full-blown credit crisis appears to have abated for now after fast action from central banks.

Key points from the quarter:

- January 2023 was the strongest opening month for the Australian market in over 30 years. Global markets (MSCI +6.5%) were also up as the pessimism in December 2022 gave way to "soft landing" euphoria on positive economic data (e.g. softening US PPI) and the China reopening.
- The equity market retreated slightly in February during one of the more interesting reporting seasons. Global markets fell as the "landing" pendulum swung back to "hard".
- The reporting season had a lot of moving parts. From a macro perspective:
    - Revenues were stronger than expected, reflecting the continuing strong economic backdrop (volumes) and cost recoveries (price);
    - Cash flows generally struggled to keep up as working capital levels increased;
    - Operating margins were pressured as wages, raw materials, energy costs and higher interest expenses continued to impact and hence;
    - Companies generally gave cautious guidance as 2H23 volumes thus far declined, particularly in the building and retail sectors
- Lastly, March was an extraordinary month whereby the collapse (and near collapse) of a handful of US regional banks, and the hastily arranged takeover of Credit Suisse by UBS, sent a shockwave through global markets. After falling -6% from the early month high, the Australian equity market closed the month down only 1%.

FUND COMMENTARY

Over the quarter the performance of portfolio companies reflected the macro influences of strong performance from USA exposed cyclicals – Aristocrat, Reece, and James Hardie – as a potential pause in rate hikes would benefit the housing market. Meanwhile the poorer-performing portfolio holdings were mostly interest-rate sensitives – Charter Hall, Macquarie, NAB, and CBA – which also fell on worries of banking contagion and commercial real estate exposure.

Notable portfolio changes include:

- We have increased our position in CSL. It is now a top-10 active holding. Industry fundamentals are improving, with plasma collection costs falling and competitor Grifols (20% market share of IG market) running into balance sheet issues.
- We have increased our position in Tabcorp and exited The Lotteries Corporation following a strong maiden 1H result for TLC. Nearly one year on from the demerger of The Lotteries Corporation from Tabcorp, the demerger has been a success with the combined businesses being valued at $6.20 post demerger vs $5.40 pre. At current valuations, we find Tabcorp the more compelling prospect. The history of demergers suggests the less glamorous business typically ends up being the stronger performer over time, likely due to low starting expectations, improved financial strength and a recut of management incentives on demerger. We note Tabcorp's CEO has purchased $2m worth of shares on market over the last 10 months.
- We have added to our position in Mineral Resources, with softer lithium prices weighing on the stock. The lithium industry cost curve is nascent and steepening quickly, which renders the position of Mineral Resources' lithium assets on the far left of the cost curve more valuable.

OUTLOOK

The March quarter has culminated in a pivotal moment with the failure of SVB/Credit Suisse. The panic in financial markets has subsided but the narrative has swung to financial resilience and hence a possible pause by central bankers in their rate hiking program. Consensus is that policy makers will wait to survey the landscape for any other areas of potential severe stress. Meanwhile we continue to be pleasantly surprised by the performance of the S&P and ASX indices – the total return since the first interest rate increase in May 2022 is +3.2% – a remarkable outcome after the most aggressive rate hiking program ever.

That said, it's logical to assume that things get tougher from here despite nothing major having 'broken' in Australia… yet (apart from a handful of small, privately owned building companies). The mortgage reset, higher energy costs, high rents, and general services inflation must put pressure on consumer spending at some stage. Offsetting these bearish factors are household savings, a buoyant employment market, and strong immigration. The Australian economy over the last three decades has oscillated between boom and "muddle through", and we think we look set to muddle through once more.

Of course, the economy is not the equity market. While we are not super-bearish on the economy, high valuations and still record high margins and returns make the investment case for many stocks uncompelling. The narrative for equity markets used to be "there is no alternative". Now there are many alternatives that in most cases offer superior yields to the low-growth dividend stalwarts of the ASX. The case for equities remains stock-specific and rests on either earnings growth or capital returns. The returns from investing in the equity of a business will always surpass its debt if the earnings power of the business today is not reflective of the earnings power it will enjoy in the future. This view encompasses not just the obvious growth "darlings" (which in our portfolio include stocks like CSL), but also turnarounds like Tabcorp and QBE. As for capital returns, the one bright spot in all the doom and gloom in the ASX is that corporate gearing remains fantastically low. We expect capital returns may smooth the experience of investors in a downturn. As famed US value investor David Einhorn said during the quarter – "It seems companies will more and more have to provide investors with a return *through their own means* i.e., higher/special dividends and/or buybacks."

STOCK STORY - QBE INSURANCE

(Joe Wright – Senior Analyst)

QBE – Quality management and strong cycle leading business turnaround

QBE is a global commercial insurance provider. The stock is a position we first added to the portfolio in September 2022. This is a company that for a long period had failed to pass almost every step in our process – business quality, financial strength, management quality and valuation. The impetus to revisit the stock was twofold – we liked the medium-term outlook for insurance pricing and the company announced the appointment of a new CEO with a fantastic reputation, Andrew Horton.

Insurance pricing is cyclical and alternates between periods of soft and hard market conditions. Several years of above-trend catastrophe events (CATs), as well as covid-related business interruption claims and the return of broad-based inflation, has seen the commercial insurance market tighten considerably. The net has been a prolonged period of premium rate growth not seen since the early 2000s. The cycle looks poised to continue (albeit at a lower rate of growth) as insurers digest and push through the impact of reinsurance rate increases, and continue to price for an inflationary environment. (refer to the premium rate change chart over time at the end).

QBE specifically has spent much of the past decade trying to digest an untethered period of acquisition spending that took place under former CEO Frank O'Halloran. Insurance is ultimately a people business and acquiring a range of large and small businesses all over the globe in a short period meant QBE lost track of the quality and exposure of its underwriting. The issues were particularly acute in North America, where the combined operating ratio of the region has remained above 100% for much of the past ten years. However, despite some of the headline results, there have been incremental signs that the underlying quality of QBE's business has been improving – divestment of underperforming exposures, poaching quality underwriting teams and transactions to de-risk reserves.

QBE's calendar year 2022 result arguably represented the first reporting period in which investors could plainly see the improved operating performance of the business. Gross written premiums (GWP) grew 13%, inclusive of an average group-wide renewal rate increase of 8%. The company reported GWP growth of 13% constant currency and an underlying combined operating ratio (COR) of 93.7%. Pleasingly, QBE's North American division reported a COR of 98.9%, the division's first profitable result since 2018. The result in North America came despite a weaker-than-average year in the crop insurance business and is consistent with management's focus on portfolio remediation in property programs and growing the retail business to drive scale benefits. At a group level, cost discipline and operating leverage (in a strong rate environment) saw a material improvement in the company's expense ratio, from 13.3% to 12.4%. CATs came in line with November guidance, albeit ~$100m (10%) higher than the original FY22 allowance. QBE reported a 4.1% running yield for the fixed income portfolio to end the period, which is clearly a material tailwind for FY23 (and will support QBE's expectations of a mid-teen ROE). QBE's regulatory capital ratio increased from 1.75x to 1.79x, with debt to total capital reducing from 24.1% to 23.4%, the lowest level in over a decade.

We continue to believe QBE is underearning as margins for both the North American business unit (sub-scale, bad underwriting), and more recently the Lloyd's syndicates (pandemic business interruption, catastrophes), have dragged on group performance. Industry pricing trends remain favourable, which should drive positive operating leverage, and the recent step-change in investment portfolio yields (as cash rates have lifted rapidly around the world) should see return on equity remain comfortably in the double digits on a three-year view. To date Andrew Horton has demonstrated a sensible approach to growth and risk management, and for all of these reasons QBE still looks attractive to us at ~9.5x P/E.